UNISON Briefing
January 2024

IFS Pensions Review: state pension report

In December 2023 the Institute for Fiscal Studies (IFS) published the first report in its planned 18-month review of the UK pension system. The review is significant because the IFS aims to influence the pensions policy of the current and future governments. The first report focuses on the state pension.

Importantly, the IFS rejects the idea of a cap on state pension spending. In March 2023, the State Pension age Review set up by the government and undertaken by Baroness Neville-Rolfe recommended a limit on state pension-related expenditure of up to 6% of GDP. The IFS describes this proposed cap as badly designed due to its inflexibility and unfairness to larger birth cohorts. One of the IFS's key findings is that the cap should not be implemented (p. 11). It is very welcome that the IFS has reached this conclusion, as it provides scope for a generous state pension, without an arbitrary financial rule being applied as an excuse for cuts.

The IFS goes on to usefully highlight the unfair impact of increases in the state pension age, as it is lower income people who are disproportionately affected. Poorer people have lower life expectancy and rely more on the state pension for income in retirement, so the effects of raising the state pension age are very regressive. The IFS sets out the view that the state pension should never be means tested, and this is also a position that we support.

However, the IFS report argues for changing the way the state pension is uprated. UNISON supports generous uprating of the state pension as it provides the foundation of workers' retirement income and it needs to retain and increase its value for future retirees who often do not have access to good defined benefit workplace pension schemes. The IFS proposes moving away from the current 'triple lock' - where the state pension is uprated annually with the highest of CPI inflation, earnings growth or 2.5%. Instead, the IFS suggestion is to just increase the state pension with earnings. They do include a kind of 'back-stop' of using CPI where it is temporarily higher than earnings growth, but our understanding is that these inflation-linked increases are effectively 'borrowed' from future earnings growth. It is not a proposal for a 'double lock' but a proposal to only increase the state pension with earnings over the long term.

The IFS report provides a very neat graph (p. 86) to show how its proposal works over the 'normal' economic cycle. However, if applied to the actual figures since 2012, where CPI has been higher than earnings growth for 7 out of 13 years, it seems that had this 'earnings-linked' proposal been in operation, the state pension would not have gone up by the same amount as earnings growth in any one year. It would also have produced a lower total increase in the state pension over this period than under the triple lock. We calculate that the application of the triple lock would have produced a cumulative percentage increase of 57%, had the IFS proposal been in place the figure would have been 45%. Table 1 (below) presents how the IFS proposal might have worked had it been applied to this turbulent period.

Table 1: Application of IFS state pension indexation proposal to the period 2012-24

Figures highlighted in green would have been applied according to our understanding of the proposal and calculations.

		Application of IFS proposal Link to average earnings (with CPI back stop)			
Year	Increase in State Pension under the triple lock (from April) (%)	Average earnings growth (previous May-July)	CPI (previous September)	Cumulative balance ∑(earnings growth – CPI)	
2012	5.2	2.8	5.2	-2.4	
2013	2.5	1.6	2.2	-3.0	
2014	2.7	1.2	2.7	-4.5	
2015	2.5	0.6	1.2	-5.1	
2016	2.9	2.9	-0.1	-2.1	
2017	2.5	2.4	1.0	-0.7	
2018	3.0	2.2	3.0	-1.5	
2019	2.6	2.6	2.4	-1.3	
2020	3.9	3.9	1.7	0	2.6
2021	2.5	-0.9	0.5	1.4	
2022	8.4*	8.4	3.1	0	7.0
2023	10.1	5.4	10.1	-4.7	
2024	8.5	8.5	6.7	-2.9	

* In 2022 the government did not apply the triple lock, increasing the state pension with CPI (3.1%) rather than the higher earnings growth figure (8.4%).

While we are not convinced by the IFS's state pension indexation proposal, the IFS has a useful perspective on the state pension age and the proposed spending cap, and the report will be an important reference point for the pensions policy debate.

A fundamental concern we have is with the inadequacies of workplace pension provision, with most workers now being in defined contribution pensions with low contribution rates.

We will be keen to see future IFS reports on this aspect of the pensions landscape and believe that it will be necessary to revisit the role of the state pension, and the government more widely, in addressing a serious shortfall in the pension entitlements workers are currently building up.

References

IFS (Institute for Fiscal Studies) (2023) *The future of the state pension*. December. https://ifs.org.uk/publications/future-state-pension

DWP (Department for Work and Pensions) (2023) *State Pension age Review 2023*. March. https://www.gov.uk/government/publications/state-pension-age-review-2023-government-report/state-pension-age-review-2023#executive-summary